

THE HIGH-TECH STRATEGIST

Issue #386

Published Monthly Since 1987

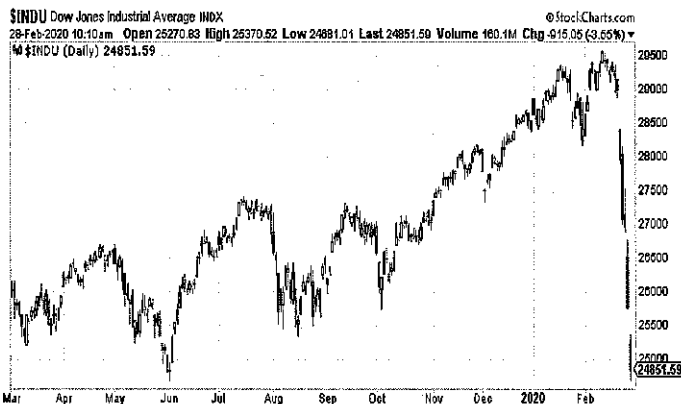
Editor: Fred Hickey

March 1, 2020

DJIA 25409.36 NASDAQ 8567.37 Gold 1586

Once Again the Music Stopped (without much warning)

Last month's newsletter was titled: "Will Coronavirus Deflate the Stock Market Bubble?" As you can see from the chart below of the Dow Jones Industrial Average on midday Friday (the S&P 500 index chart looked the same), it now appears that the answer will be a resounding... yes! Up until mid-February (the S&P 500 index peaked on February 19), investors had been in denial about the seriousness of the impact of the virus (since named Covid-19), as they continued to drive the bubble to greater heights.



Throughout the first half of February, I was on Twitter tweeting out important data concerning the virus and taking serious flack for pointing out the "insanity" of what I was seeing. Here's one of my tweets from Feb 19 (peak bubble day): "Hello Fed! Anyone there seeing any bubbles yet? Virgin Galactic (SPCE) has quadrupled since Dec. (up another 10% pre-market) \$6 billion market cap (1,300 times sales) because we're all going to need to travel to outer space to escape coronavirus? Tesla up another 61 points (7%) this AM to \$920."

I received a response from an investment professional who advises hedge funds: "Yes it's insane, but you gotta play the game that's on the field. If index funds, buybacks, ETFs and momentum hounds are chasing the same names it's OK to play the game knowing the clock will run out. Nobody gets paid to underperform!" I don't normally reply to the many Twitter respondents (and Twitter trolls), but this time I made an exception and noted his comments sounded similar to CEO Chuck Prince of Citigroup, who famously stated in the summer of 2007 (just before the bottom fell out in the Global Financial Crisis): "When the music stops in terms of liquidity, things will be complicated. But as long as the music is playing, you've got to get up and dance." Not long after Prince made these comments, the collapse began. Citi's stock ultimately cratered

98.3% and Prince was gone from Citi by November 2007 (though with a fat \$38 million pay package).

Last week's stock market crash (Dow Jones Industrial average plummeted 3,583 points -12.4%, by far its largest weekly point loss in history) didn't provide much time for the partygoers to exit. As the Wall St. advisor said: "Nobody gets paid to underperform" so many of them (especially the computer algos) tried to get out at the same time. With stocks at record levels (using many metrics - as explained in last month's letter), buyers were scarce and the result was the fastest stock market "correction" (defined as a drop exceeding 10%) on record - just six days. Research house Bespoke Investment Group tweeted: the "S&P 500 has only been down 10% in a week four other times since WWII; October 1987, April 2000, September 2001 and October 2008." As we all know, those were tough times to be an investor.

The Fed had spiked the punch bowl in Q4 of last year with a \$400 billion increase in its balance sheet - bond purchases with money printed out of thin air (QE) and "repos." While the QE money printing continued at a rate of \$60 billion per month in January and February, virtually none of the Wall Street wildlings noticed the Fed had sharply reduced the repos outstanding from the \$256 billion peak on January 1 to just \$126 billion by last Friday. That \$130 billion drop more than offset the money flowing into the financial system via QE. Stock market bubbles always need more air to stay afloat - otherwise they collapse. The music had stopped (in terms of Fed liquidity), but the bubbleheads didn't know it. They were still partying like it was 1999.

A recent Bank of America survey showed money managers had boosted their stock holdings while slashing their cash levels to a seven-year low. Short interest on the S&P 500 index ETF fell to the lowest level since early 2007 (virtually no shorts). On February 18 the put/call ratio hit a ten-year low. Call option buying was out of control. On February 19 SentimenTrader (well known research house) tweeted on Twitter: "Over the past 2 weeks, options traders spent more than \$16 billion buying speculative calls. That's 60% more than any other 2-week period since 2000. Maybe this is a nothing-matters-forever kind of market, but holy moly." As the speculators discovered, nothing matters - until it does.

The Fed's constant interventions had created an environment of extreme complacency (and wild speculative behavior). An example of this lack of fear was this response to one of my tweets: "Because with Fed intervention, puts are about as effective as just lighting cash on fire." Here again, I thought it was important to respond: "Problem with that 'no fear' theory is Fed repos are shrinking fast, Fed balance sheet is slowing and money velocity's plummeting too. The wildlings are running on fumes - expecting the Fed will come to their rescue - but will it

be before markets collapse or after?" We now know the answer to that question too.

I had been building up my put options positions against certain tech stocks throughout February as the Covid-19 virus spread worsened and as the stock market party on Wall Street just kept getting wilder and wilder. I added to my Tesla and Apple put positions. On February 17, Apple pulled its prior guidance given on January 28 for two reasons. From the Apple letter to shareholders: "The first is that worldwide iPhone supply will be temporarily constrained." Manufacturing partner facilities "are ramping up more slowly than we had anticipated." Editor's Note: that's still a problem today. "The second is that demand for our products within China has been affected. All of our stores in China and many of our partner stores have been closed."

Last month I added puts on a number of semiconductor names that will be familiar to readers because I've owned them before. I purchased put options against Skyworks (SWKS) because over half their semiconductor sales are to Apple. SWKS also supplies many of the Chinese domestic smartphone makers such as Vivo, Oppo, and Huawei. The China Academy of Information and Communications Technology reported last month smartphone sales had fallen 37% year-over-year in January - and that was before much of the country was shut down in February (hundreds of millions of people under quarantine). China is the biggest market for smartphones in the world. China is also the world's largest end market for PCs and 90% of notebook PCs are produced in China. I bought puts against PC parts makers AMD, Intel (INTC) and Micron (MU).

The China Passenger Car Association reported that auto sales in the first 16 days of February were just 4,909 units (in all of China - here again the largest end market in the world - 50% bigger than the U.S. market), a 92% year-over-year plunge. I purchased put options against TE Connectivity (TEL), Amphenol (APH) and NXP Semiconductors (NXPI) as they're heavy suppliers to auto producers. Many other automakers outside of China have been affected, including Hyundai in South Korea, which recently suspended production at one of its factories due to the virus. Toyota said that some of its 16 factories in Japan may have to shut down in March due to supply chain issues. China is a primary supplier of auto parts and those plants are located in some of the hardest hit (Covid-19) areas in China. Logistics (shipping) is also a nightmare in China.

There are shortages developing throughout the tech world, mostly due to factory shutdowns (and slow restarts with millions of employees not yet returned to work). Multilayer ceramic capacitors and resistor inventories have reportedly fallen to 10-year lows and as a result, prices are spiking higher (as much as 50%). So far, the shortages are found mostly in chemical materials and passive components that are primarily sourced from China. This will have an effect on many manufacturers including the likes of Cisco Systems, Dell and Microsoft. Microsoft last week lowered guidance for its PC business due to supply chain issues. DRAM prices are currently rising and I would not buy puts now against MU for that reason and also because its primary competitors, Samsung & Hynix have factories in South Korea, where there are virus outbreaks.

I also bought put options against Booking Holdings (Priceline - BKNG), as the travel industry is the hardest hit of all. Businesses everywhere (including in the U.S.) are canceling conferences (examples: Facebook cancelled its annual marketing conference in San Francisco and Workday cancelled its annual sales "Kickoff in early March in Orlando, Florida. The Geneva Car Show in Switzerland was recently called off as was the smartphone industry's biggest conference - the Mobile World Congress in Barcelona, Spain (held for 33 consecutive years - over 100,000 attendees). The Tokyo Summer Olympics may also be cancelled (volunteer training has been postponed). A decision on that major event will be made in the next few weeks.

Covid-19 = Global Recession

The whole world is following the spread of this disease so I'm not going to spend too much time on it here. A month ago, when I wrote the February newsletter, there were 24,000

confirmed cases and 492 deaths - almost all of them in China. Now, four weeks later, there are more than 88,000 cases, over 3,000 deaths and 67 countries and territories with confirmed cases - several of which - including S. Korea, Italy and Iran - where outbreaks are severe. I don't know how far or for how long this epidemic will last. I truly hope it's significantly reduced in warmer weather (summer).

Nevertheless, there is no question in my mind the disruption this disease is causing around the globe will be enough to tip over the already-softening global economy into recession. Recessions cleanse the system from excess debts, malinvestments and speculative behavior and we have them in spades (record amounts) today because the major central banks of the world have intervened so often, making the problems far worse. The trillions of investment dollars already lost just in the last week will also weigh on business and consumer confidence and spending.

I'm certain the Fed and other central banks will try to intervene again with what little rate cut ammunition they have remaining in their arsenal and via more QE money printing. These interventions (another one may come as soon as this weekend) will likely cause stock markets to temporarily rally, but will not forestall the inevitable recession. Last week, as the markets plunged (and with the VIX fear gauge at 48 - very high), I sold almost all my put options (except for a small number of Skyworks puts) with the intention of buying many of them back after a central bank-driven rally. There was a sharp stock market rebound late Friday afternoon based on comments Fed chairman Powell made. Investors are expecting coordinated global central bank action imminently.

Precious Metals & Miners

These central bank actions should be very bullish for gold, silver (eventually) and the mining stocks. They had held up well throughout February (record highs for gold in many key currencies) until Friday - when they were hit hard. Many pundits attributed the metals' selloff to a 2008-like liquidity crunch, which at the time depressed gold for about four months that year before gold took off again - nearly tripling to \$1,900 over the next three years. Though there were certainly some margin calls last week, I didn't see much evidence of a 2008-like liquidity squeeze.

U.S. banks are in far greater shape than they were in 2008 (basket cases). I think it was just muscle memory - investors in gold and the miners *remembered* what happened in 2008 - and so they panicked and sold. But they'll also remember the precious metals' and miners' explosion higher as the Fed engaged in QEs 1-3. When the Fed intervenes again, I expect it will be very bullish for the precious metals sector. A U.S. recession will cause the \$1+ trillion annual U.S. federal budget deficits to soar to \$2+ trillion and I expect the Fed will elect to monetize those debts. They're interveners enthralled with themselves and their QE "tools."

Last month's newsletter was almost all tech-focused and I mentioned I would give updates in this letter on the gold miners that have recently reported quarterly results. It's a good time to do so, as the miners are still severely undervalued, despite last year's great gains. Moreover, the gold miners will be one of (if not the only) industry showing strong earnings growth this year. Goldman Sachs' chief equity investment strategist last week predicted: "U.S. companies will generate no earnings growth in 2020." Investors will take notice as miners continually report strong results. They will be the safest port in this storm.

Q4 2019 numbers for the miners were generally quite good and that was with gold averaging around \$1,480 an ounce in the quarter. As you'll see in the writeups, many of the miners are now gushing free cash flow and sharply raising dividends. Investors (and computer algos) will eventually notice that too. Additionally, in the recessionary period ahead, the miners' costs will likely remain under control (some may even decline - as happened in the 1930s). Gold is now over \$100 higher than in Q4 - which means even bigger cash flows and earnings for the current quarter. Gold miners today at \$1,585 gold and around \$900 average AISCs (all-in sustaining costs) have higher

margins than in any year (on average) during the 2000-2011 great gold bull market – yet the miner's stocks are nowhere near the levels they attained back then. In 2011, the HUI gold miner stock index was over 600 and today it's just 216. We can make a lot of money when this disconnect is corrected. I also believe we'll be seeing record prices for gold (in U.S. dollars) as the Fed prints ever more money and debases the dollar.

Barrick Story Convinces More Investors

The new CEO at Barrick (GOLD), Mark Bristow, has a reputation for not missing estimates and the reputation is well deserved. In Q4 Barrick's gold production came in at the upper end of its guidance range and its copper production was above guidance. Barrick beat earnings estimates (by 3 cents per share) and raised its quarterly dividend by 40% to 7 cents per share (from 5 cents). The yield is now 1.5%. Barrick CFO Graham Shuttleworth on the dividend announcement: "The board believes the dividend increase is justified by the significant reduction in net debt and strong balance sheet, together with the growth in free cash flow supported by a robust 5-year plan which we have shared with the market." It was the third dividend increase over the past year. On the conference call, Bristow stated, "this is what we said we would do" (raise the dividend). He also said Barrick "will only pay dividends that are earned" and "we don't want to go backwards only forwards."

Barrick's gold costs per ounce in the quarter fell from the prior quarter. Cash costs were \$692 an ounce and AISC costs were \$923 an ounce, down from \$984 an ounce in the prior quarter. With a realized gold price of \$1,483 an ounce in Q4, Barrick generated a healthy amount of cash flow and margin. Considering that gold is \$100 an ounce higher now, Barrick's cash flows (and margins) should continue to rise. We can expect more dividend hikes in 2020.

Barrick's net debt was \$11.85 billion in 2012 and now it's down to just \$2.2 billion at the end of 2019. Net debt was nearly halved (down 47%) over the past year. On the conference call, Bristow noted there wasn't a lot more left to do (in cutting debt) as much of the remaining debt wouldn't mature for quite a while, some of the remaining debt would cause Barrick to incur penalties to retire it early, and some was at low interest rates. Bristow expects Barrick to exceed its target of \$1.5 billion in asset sales in 2020 (after divesting \$1B in assets in 2019). Bristow told a Bloomberg interviewer last month that Barrick was "eminently comfortable" to continue hiking the dividend. He also noted that a higher dividend was key to attracting investors to the stock. In the current yield-starved world, a steady rate of dividend hikes should be very well received by investors. The stock popped nicely following the Q4 report.

Barrick also last month issued its annual reserve and resource update. Barrick reported an attributable gold mineral reserve increase of 14.5% (at a 7.7% higher grade than the year before) for a total of 71 million ounces (assuming just a \$1,200 an ounce gold price). On the conference call, Bristow noted gold production worldwide is expected to peak either this year or next (due to sharply reduced exploration in recent years and a lack of major discoveries) and by 2029 global gold production may be 30% below what will be needed by the market. He stated that at a \$2,000 gold price, Barrick would show 170 million ounces in reserves (nearly 100 million more ounces than they reported last month).

The only negative for me in this story continues to be the location of some of its mines (particularly in Africa) where there are geopolitical issues (including difficult governments). However, Bristow has a lot of experience in that area of the world and at his prior CEO role at Randgold, he was quite successful dealing in those countries. Still, Bristow is slowly divesting some Barrick's mines in more difficult regions of the world. On the conference call he also noted that Barrick was "underinvested in Canada," hinting that if Barrick did engage in acquisition activity, it could be in that country. That was encouraging to hear as I own a lot of smaller Canadian-based miners that are attractive takeover candidates.

Bristow Calls Out Donlin Mine On Conference Call

NovaGold (NG) owns 50% of the Donlin gold mine with Barrick owning the other half. Though Donlin is not located in Canada, this massive undeveloped mine is close enough – in nearby Alaska. Donlin is a huge project - 39 million gold ounces grading at 2.24 grams per ton (the grade is twice the industry average) and a 27-year mine life (at least). The mine is now fully federally permitted and NovaGold is in the process of obtaining all the state permits, several of which were received in 2019. However, developing the project would require a very large upfront investment, so it is clearly beneficial to have a partner the size of Barrick. When Barrick CEO Bristow came in and the took the reins last year, there was some doubt as to what he might do with Barrick's Donlin ownership share. I had heard from a good source recently that Bristow, after studying the project, viewed it favorably, but the proof came during Barrick's conference call when he specifically called out the project in the midst of his mine operations review (a very pleasant surprise for me).

Bristow: "A quick comment on Donlin, Donlin Creek in Alaska. It offers huge optionality to the gold price across multiple gold price cycles in an excellent jurisdiction. But it faces some challenges that we and our joint venture partner, NovaGold, intend to address." "To this end, we have updated the geological and resource models which have identified areas of higher grade that could improve returns for the overall project. And importantly as well, we need to frame that to those geological ore bodies properly because that will set the rate in which we can mine, which will set the answers that we can theoretically produce, which will then govern what ounces, what capital we have to spend to deliver the return on a back-to-front way." "And so we are busy with a phased program this year." "We'll drill it up, remodel it, check out the changes, drill it again. We'll do a couple of those through the year or certainly through the summer." Bristow is a very methodical CEO, and he appears to have a lot of interest in Donlin.

Agnico Eagle's Stock Gets Slammed

Agnico Eagle (AEM) was a big winner for me last year and as my largest position, its 53% gain in 2019 was a significant contributor to my huge overall portfolio gain. However, as readers know, I don't get caught up in the excitement of big up moves because I know that with higher prices it usually means higher risk (a concept the FANG buyers paying up for \$1+ trillion dollar valuations seem to know nothing about). Therefore, as some of my big winners (including Kirkland Lake) soared last year, I slowly reduced position sizes in them. Readers know that by year end I'd built up a sizeable cash reserve to be used for "opportunities."

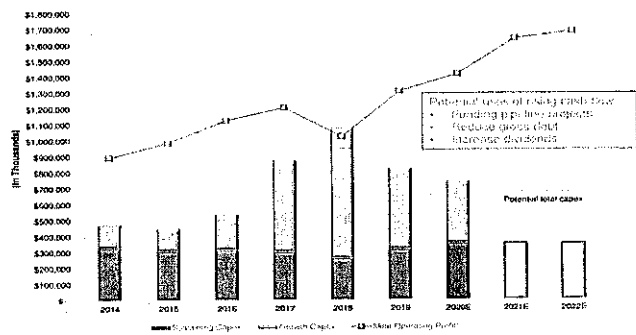
In December, I put some of that money into battered, hated, high-dividend paying energy stocks (unfortunately, they've continued to get battered) but the rest of the cash I've sat on. AEM reported very strong results for Q4 (record quarterly gold production, revenues up 40% year-over-year, massive operating cash flow - \$1.08 per share - and a slight "beat" on earnings). With the cash flow that AEM's now generating and even more in upcoming years (see the chart below sourced from AEM's Q4 presentation), AEM announced it was raising its dividend by 14.3% to 20 cents a quarter (80 cents per year for a yield of 1.7%).

AEM has now raised its dividend for six consecutive years. As you can see from the chart, with much of AEM's new mine building having already occurred (see the significantly shorter bars), AEM's cash flow in upcoming years is expected to continue to soar (see top line). That should lead to even more dividend hikes, as well as a reduction in debt – which is not very high to begin with.

Despite all this "good" news, a 3½% cut in the 2020 production forecast (production is still expected to climb 18% through 2022) and an increase in unit cost growth (especially in 2020 – declines in unit costs are expected in 2021 and 2022), sent some AEM investors (especially computer algos and momentum adherents) into a tizzy, crashing AEM's stock by 15%. Mining is not an easy business, and as the saying goes,

Agnico Eagle's Growing Business Positioned to Generate Rising Free Cash Flow

AGNICO EAGLE



Free Cash Flow is defined as operating cash flow minus capital expenditures. Potential Free Cash Flow is based on a price of \$1,300 per ounce. Fourth Quarter and Full Year 2019 Results.

“stuff happens” in the mining business. There were a few problems that caused the (mostly 2020) shortfalls and most of them should be very short-term in nature. Startup issues at the new Nunavut mines (Meliadine and Amaruth) are hurting results. Meliadine’s mining and back end of the mill did well, but the front end of the mill had a problem with a piece of defective equipment. That problem should be fixed in Q2 2020. AEM actually increased Meliadine’s production forecast for 2021 and 2022 due to the company’s decision to advance the Phase 2 expansion at Meliadine.

Similarly, at Amaruth there has been a slower than expected ramp up of mining activities. Part of the problem was the record amount of rainfall late last year in eastern Canada (affected a lot of other miners as well), which reduced AEM’s access to certain higher grade sections of the Whale Tail pit (AEM had to perform extensive dewatering), as well as lower than expected productivity at the mine (logistics of moving mining equipment and people from the main Meadowbank complex to Amaruth). But the problems will mostly affect Q1 of 2020 and according to management, productivity has been progressively improving, month-by-month, and they expect by Q2 Amaruth should be “at a normal mining rhythm pace.”

The more longer-term problem was at LaRonde where AEM had expected to begin mining the higher-grade West Mine area. Due to some seismic activity in December, the mining team will be adding structural support to the mine in early 2020 before beginning to mine in that area. In the meantime, AEM will be mining from the (lower grade) East Mine. Per AEM: “This impact (lower production and higher total cash costs per ounce) will be concentrated in the first quarter of the year as ground support infrastructure work is completed. Changes in the mining sequence related to the merging of the mining pyramids in the East and West mine areas is also expected to impact production in 2020 and into 2021. Production is expected to increase (and costs decrease) in 2022 and beyond, though AEM’s management is planning to mine at a bit slower rate due the deeper depth of the mine (a prudent safety move).”

I’ve been an investor in AEM’s stock for many years. These types of problems crop up every once and a while. Mine startups are especially tricky times. However, AEM’s management, in my opinion, is one of the best in the business, and past stumbles have been buying opportunities. Readers may remember years ago when AEM completely shut down their Goldex mine due to structural issues (AEM has an excellent safety record), crashing the stock. Today, the Goldex mine is a standout performer and produced a record amount of gold in Q4. AEM’s stock was also hit after a fire at its new Meadowbank mine’s kitchen (a wolverine caused it to completely burn down) and again when Meadowbank’s scale was cut back. Meadowbank was AEM’s first mine in Nunavut and now the Nunavut region holds the most upside for the firm with the high-grade Meliadine mine ramping as well as Amaruth – and there are many more opportunities as well.

Though I am mindful that the negative momentum may continue to pressure the stock for a while, I’ve taken advantage of the overreaction to buy back almost half of what I’d sold and

have lots more cash reserves remaining if the stock continues to fall. Having watched this AEM management team for many years, I know they’re conservative forecasters and I’d expect they’ve taken advantage of the production shortfall to set estimates that should be exceeded throughout 2020. I was joined as a buyer following the selloff in the public market by Agnico President Ammar Al-Joundi, who purchased 2,000 shares, independent director Mel Leiderman (2000 shares) Sr. VP Jean Robitaille (2000 shares) and CEO Sean Boyd (5,000 shares).

Hecla – A 2021 Growth Story

Hecla’s made a lot of progress since their near-death experience last year (stock fell to \$1.31 and there were worries about the company’s ability to pay off maturing debt) following their ill-advised acquisition of Klondex in mid-2018. Hecla now refers to Klondex’s gold mining assets as their “Nevada” assets. Thankfully, Hecla (HL) was able to stem the bleeding and drastically slash spending on the Nevada mines in the first half of 2019 and in the second half start to show significant free cash flow again (\$57 million of cash provided by operations and \$33 million of free cash flow net of capital expenditures in Q4).

This progress enabled HL to significantly strengthen the company’s financial position, reducing their net debt-to-EBITDA ratio from around 6x in Q2 to under 3x by the end of the year. HL reduced their net debt by about \$136 million (23%) from the high at mid-year. Moody’s upgraded HL’s bond rating (to B3) and the culmination of all this progress was the successful sale in mid-February of \$475 million of senior notes due in 2028, replacing the senior notes due in 2021 and thus significantly reducing concerns over the company’s viability. HL paid a price – a 7.25% rate versus the 6.875% notes it was replacing (\$500 million).

HL’s management will be doing studies on the Nevada assets (particularly Fire Creek) that will “take 1 to 2 years” and after that, assuming they can prove a good return on investment, there will be additional time involved in a permitting process. Therefore, though HL’s management still believes “these mines and exploration targets that we bought when the gold price was \$1,200 an ounce will have great value in the future” (we’ll see), the Nevada assets will basically be a non-factor for HL for at least a couple of years.

That leaves Hecla with four key producing assets – all located in North America. The Greens Creek Mine is the company’s flagship mine and is a steady producer. The other three mines will be in transition in 2020 but should kick into a higher gear by 2021. HL forecast they’ll produce 11.1 million to 12.1 million ounces of silver in 2020 – slightly less than in 2019. HL’s Lucky Friday mine, which had been almost completely shut down due to a long labor strike (almost three years but now settled) will have a “building year” and COO Lauren Robert observed on the conference call that HL does “not anticipate the mine to become cash flow positive during the restart.”

Lucky Friday will be shut down for most of the first quarter (capital projects before the restart) and then the “ramp up and recall will start in earnest in Q2.” As you can see, HL’s first half could be weak (possibly providing a chance for me to increase my position). Once Lucky reaches full production late in 2020, HL expects to see much higher grades and the cash flows will be significant (as they were before the shutdown – it was Hecla’s second biggest mine). Lucky Friday will produce 1 million more ounces in 2020 than in 2019, but the mine will really kick into gear in 2021 at full production. Last year, Hecla increased its overall silver reserves by 11% - including a 22% increase at Greens Creek.

Those additional ounces from Lucky should offset a drop from its San Sebastian mine in 2020 (oxides will be mined out). Roberts explained: “2020 is a transition year for San Sebastian.” If HL goes ahead with a production decision for the Hugh Zone (sulfides - study should be completed in Q1), “Starting in 2021, it should be a solid cash flow contributor to the portfolio for about another six years,” Roberts said. So far, the sulfide test mining and recoveries have gone well.

Casa Bernardi (a gold mine Hecla owns in Canada) should also see improvements as 2020 progresses as HL “starts

producing previously developed 148 Zone (East Mine) ore in the first quarter and to access newly developed ore by the end of the year.” “Historically, the East Mine has been higher grade than the West Mine and this is reflected in the 148 Zone, which has about 50% higher grade than the average underground grade,” Roberts stated

As you can see, 2021 is when HL’s growth should resume again and 2020 is a transition year. I’ve had great success with Hecla’s stock over the years, making it one of my top five positions in 2015, watched it more than triple in 2016, sold it all close to the top in 2017 (putting all the HL proceeds into Kirkland Lake in the mid-\$6 range – and we all know what happened then), got back into HL last year for some more good gains and have since cut that position back again following a sizeable up move (though I’ve kept some too). On any significant sell-offs that might occur in 2020, I expect to build up that HL position again in anticipation of much stronger production performance towards the end of this year and into 2021.

Opportunity With New Gold - Though With High Risk

The relatively new management at New Gold (NGD) inherited quite a mess from the prior management at the company’s Rainy River Mine. Since taking over, they’ve had to finish building the mine and address a number of issues over the past year in order to “significantly reposition this asset for success.” Last month, Renaud Adams and team came up with an entirely new “life of mine plan” for Rainy River (as well as for its solid New Afton Mine) which reduces the size of the Rainy River pit to be mined and lowers the remaining life to 8 years, but eliminates the mining of 4 million waste tons. The lowered costs should allow the mine to become cash flow positive in either the third or fourth quarter of this year and significantly more so for the remaining years. Rainy will be mining the medium to high grade ore, while stockpiling the lower grades.

New Gold held a 2 hour and 38-minute marathon “technical” conference call last month to explain the new plan in great detail. I listened to every minute of it and came away impressed. Adams stated the plan was “achievable and provides for further upside.” As I’ve noted before, Adams had a great record at Richmond before selling the company to Alamos. He also declared that he has “confidence we can beat this plan.”

Adams: “What I like about this plan as well is it shows five consecutive years of production growth and sustained growth, from the 250 (thousand ounces level), achieving the 350 (thousand ounces) towards 2025 and sustained again in 2026.” “And as you grow, your costs will go down.” Under the plan, Rainy River’s AISC cost is expected to average \$967. Assuming a \$1,300 gold price, NGD estimates Rainy River’s cumulative cash flow to be \$557 million and its after-tax net present value at \$421 million. At \$1,550 gold, the cumulative cash flows are expected to be \$1.096 billion and the after-tax net present value to be \$859 million. As you can see, a huge sensitivity to the price of gold (and some silver).

New Afton’s net present value calculations (New Afton is more sensitive to copper prices) ranges from \$735 million to \$766 million. At \$1,550 gold, the combined net present value would be \$1.862 billion. Currently New Gold’s market cap is \$540m – but one has to add back net debt at \$631M to come up with an \$1.17B. As you can see, NGD’s current enterprise value is significantly less (37%) than its net present value at \$1,550 gold and that does not include any value for its Blackwater project which had been valued by analysts as high as \$1 billion when gold was near its top in 2011-2012.

However, NGD has to execute on the plan. NGD also had a second hurdle - to find a way to refinance the \$397M in senior unsecured notes due on November 15, 2022. Last week NGD announced a \$300 million financing agreement with the Ontario Teachers’ Pension Plan. Under the deal, New Gold will receive \$300 million in cash proceeds when the deal closes (likely by the end of March) and Ontario Teachers’ will acquire a 46% free cash flow interest in the New Afton mine and an option to convert the interest into a 46% joint venture interest in four

years. It looks to be a good deal for both parties, but in New Gold’s case, it essentially puts to rest the issue of the November 2022 note payment. The market reacted very positively as New Gold’s stock jumped to \$1 on the news.

As I’ve been saying for some time, this is a very high risk/reward kind of stock. I did well (reduced some of my prior years’ NGD losses) by buying NGD a bit below 80 cents and then selling some at higher prices last year. NGD declined about 10% immediately after the new life of mine plan and Q4 results were released last month. I took advantage of the drop (back below 80 cents) to repurchase much of what I’d sold last year.

Wesdome – The Hits (Drilling) Keep On Coming

Wesdome announced excellent drill results (high grades and wide lengths) first for its Eagle River Mine (February 12) and then again for its Kienna Mine Complex (February 19). I repurchased last month half the shares I had sold at the end of 2019. Wesdome will report quarterly results on March 10.

Solid Results at Alamos

Alamos reported solid Q4 results with slight beats on the top and bottom lines. The company reported record cash flow from operating activities of \$77.8M (up 64% year-over-year) and a record \$85.7M before changes in working capital (22 cents per share – that’s a lot on a \$7 stock). The Young-Davidson mine recorded its second-highest quarterly mining rate in its history and the construction of the lower mine “is in its final stages.” The tie-in of the lower mine with the upper mine has commenced, “and remains on schedule” for completion in June. Following that tie-in, Alamos will start seeing higher production, lower costs and significantly higher cash flows beginning in the second half of this year. Results will be lower in the first half due to this project. Once it’s completed successfully, I’ll likely add to my position.

Alamos’s most exciting mine is clearly Island Gold, which saw a 21% increase in its reserves last year (1.22 million ounces at very high grades of 10.37 grams per ton). Island Gold’s inferred mineral resources jumped 46% from a year ago (2.3 million ounces at 13.26 grams per ton). On the conference call CEO John McCluskey declared: “So what we have here is a deposit that’s now looking like 3.5 million ounces going to 5 million ounces and (it’s) going to last for a very long time.” As noted, these are very high grade, low-cost ounces that will generate a lot of cash for Alamos. The mine plan for Island currently has 15 years remaining – and it’s likely to last longer than that. With \$183 million of cash on its balance sheet, no debt and strong cash flows expected starting in the second half, AGI shareholders should look forward to higher increases in the dividend (currently just 1% - but recently hiked by 50%) as well as the continuation of its significant share buyback program.

Pan American Silver- Record Cash Flow & 43% Div Hike

Pan American Silver (PAAS) reported very strong Q4 results. Adjusted earnings per share (33 cents) bested analysts’ estimates (22 cents) though there was an investment gain involved. PAAS generated a record \$129.5 million in net cash from operating activities in the quarter (over 60 cents per share), increased its dividend by 43% (to 20 cents per share annually) and significantly paid down debt (by \$40 million). Last month PAAS reported more excellent drill results for its La Colorada skarn discovery that will allow them to further increase their already enormous 72.5 million ton resource estimate. PAAS forecast 7% silver growth production in 2020 and 16% growth in gold production.

Kirkland Lake –Fosterville Concerns Overshadow Results

Kirkland Lake (KL) reported tremendous Q4 results. Revenues of \$412M were up 47% year-over-year, adjusted earnings per share of \$185M (88 cents per share - a 3 cent “beat” of analysts’ estimates) increased 76% year-over-year and free cash flow jumped 48% to \$133 million. Cash at year end was \$707M (a 133% jump over a year earlier). Kirkland increased their quarterly dividend twice in 2019 to 6 cents per share in Q4. “We plan to substantially increase these efforts, including doubling our quarterly dividend to \$0.125 per share (50 cents per share annually, 1.6%), effective the second quarter of 2020, and

committing to buying back 20 million shares (nearly 10% of their shares) over the next 12-24 months," said KL CEO Tony Makuch.

However, all of this unquestionably great news was overshadowed by continuing concerns over the sustainability of the extremely high-grade production from the Swan Zone at the Fosterville mine in Australia. KL reduced their reserves at Fosterville by 637,000 ounces in 2019 – due mostly to depletion. Kirkland forecasts production at Fosterville over the next three years of around 600,000 ounces per year - similar to the 619,000 ounces produced in 2019. The worries are about 2023 and 2024 and those concerns have been weighing on the stock for some time now.

It's a reality that the Swan Zone has a limited life and mine zones with 40+ grams per ton are very rare. However, investors have slashed nearly 37% off KL's value from last year's high (when gold was under \$1,500 an ounce). At \$32, KL's market cap is \$9.5 billion and after adjusting for the \$700 million of cash on the balance sheet, its enterprise market value is \$8.8 billion. KL expects to generate "well over half a billion dollars of free cash flow this year." One could expect that level of free cash flow (at least) to continue through 2022.

KL recently purchased Detour for \$3.3 billion (less than \$275 per ounce for the reserves), the company believes they got a deal with lots of upside (lower costs, higher production and more reserves) and Tony Makuch stated on the conference call that Detour may generate "as much cash flow as all the other assets combined." KL's Macassa mine in Canada had some tremendous drill results in 2019, significantly increased reserves (very high grades) and has "huge upside." KL has moved forward the completion date of the #4 shaft project by about a year and KL projects production from Macassa will jump from around 250,000 ounces in 2020 and 2021 to 330,000 ounces in 2022 and to over 400,000 in 2023.

Fosterville is not going to go away, though it's likely there won't be 40 grams per ton Swan zones – but one can't rule that out either, as there's still lots of drilling targets including primary ones at "the Lower Phoenix System, Cygnet, Harrier, Robbins Hill and a number of regional targets." In some of these locations KL has seen signs of potential high-grade zones, including quartz and visible gold. Robbins Hill "has the potential for production to commence in 2023" and KL started it with an initial reserve of 218,000 ounces. The Robbins Hill deposit is "open down plunge." I increased my position a bit following the earnings report.

Osisko Mining's New Mineral Resource Estimate

Osisko Mining updated its mineral resource estimate for its Windfall gold deposit to include the latest (extremely good) bulk sample results. The indicated resource is now 1.21 million ounces averaging 9.1 grams per ton and the inferred resources are 3.94 million ounces averaging 8.4 grams per ton. Combined, that's 5.15 million ounces of gold, which Osisko described as "world-class scale." Importantly, "the mineral estimate is entirely above 1,200 meters," meaning it's not too deep to economically mine. The criticism on Osisko has been the deposit may be "too deep." "Strong potential for expansion remains in the known Lynx zones, the majority of which are open along strike to the northeast and down plunge below 1,200 meters," CEO John Burzynski said. Osisko's Triple 8 (high grades) discovery, "at approximately 1,500 meters vertical depth, was not included in the current mineral resource estimate but hosts excellent potential to add significant ounces with additional drilling." Kirkland Lake already owns around 13% of Osisko Mining. KL certainly has the ability (and possibly the need) to acquire the rest, and if they wanted to include Bonterra Resources, they'd have quite a sizeable district, with high grades. Late last week during the selloff I added to my Osisko and Bonterra positions.

Newmont Mining – Institutional Favorite (& in S&P 500)

Newmont, the world's leading gold company, reported excellent Q4 results, helped by average realized gold prices that were up 20% from a year earlier (from \$1,233 an ounce to

\$1,478). We can anticipate even better results ahead from cost improvements Newmont's management is bringing to the Goldcorp assets. On the conference call, when he was asked about the Goldcorp acquisition, CEO Tom Palmer excitedly exclaimed: "It's a fantastic acquisition! Those assets are terrific ore bodies. There's excellent infrastructure and they are in very good hands and we're going to deliver huge value from them. So it was a fantastic acquisition and I think we're demonstrating what those assets can really do when they're in the hands of an operating company like Newmont."

NEM is increasing its dividend by a whopping 76% to \$1 per share annually (2.2%). As you can see from the write-ups in this letter, there are a lot of dividend hikes occurring in the precious metals sector (likely to continue) and dividends are in much demand these days by investors striving for yield in this interest rate-barren time.

Strategy/Positioning

As noted earlier, I sold almost all my put options late last week (except for a small number of SWKS put), though I plan on adding them back after a Fed-driven rally.

My precious metals positions are my largest positions, by far. My largest miner positions are Agnico-Eagle Mines (AEM), Newmont (NEM), Alamos Gold (AGI), Kirkland Lake (KL), Barrick (GOLD) NovaGold Resources (NG) and Pan American Silver (PAAS) – not in that order. I own physical gold. I also hold call options in the iShares Silver ETF (SLV) with expirations in January 2021 and January 2022. I have medium-sized positions in Wesdome (WDO, WDOFF), Hecla Mining (HL), and Osisko Mining (OBNNF, OSK), and smaller sized positions in Bonterra Resources (BONXF, BTR) Franco Nevada (FNV), New Gold (NGD) and Pure Gold (PGM, LRTNF). I added a new name last month – Silvercrest Metals (SILV). I'll have more on SILV in future letters, but they had great drill results last month.

My cash reserves are in short-term Treasuries and the rest are in low, interest-bearing money market accounts. I own Exxon Mobil (XOM), Chevron (CVX), Schlumberger (SLB) and the Alerian MLP ETF (AMLV). I almost couldn't believe Exxon's dividend yielded over 7% last week (now 6.8%).

Fred Hickey (thehightechstrategist@yahoo.com)

One-year subscription US: Email only delivery \$150, Mail delivery \$160. Email and mail delivery \$180. One-year subscription (non-US): Email delivery \$150, Mail delivery \$195. Email and mail delivery \$215. Send U.S. check or money order to: The High-Tech Strategist. Three-month trial: \$70(US). To subscribe, please send your name, address and check or money order to: The High-Tech Strategist, PO Box 3133, Nashua NH 03061-3133

We have set up a PayPal account as an alternative payment option for a \$10 fee to cover costs. Upon request via thehightechstrategist@yahoo.com email address, we can electronically send an invoice through the PayPal system, or we can give our PayPal account email address in order to send us payment.

Information presented in this newsletter was obtained from sources believed to be reliable, but accuracy and completeness and opinions based on this information are not guaranteed. Under no circumstances is this an offer to sell or a solicitation to buy securities suggested herein. The editor may have an interest in the companies mentioned. All data and information and opinion s expressed, are subject to change without notice.